

***United States Court of Appeals
for the Second Circuit***



**APPELLEE'S
SUPPLEMENTAL
BRIEF**

76-7616

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

----- X
IN RE
FRANKLIN NATIONAL BANK SECURITIES
LITIGATION
----- X

ROBERT GOLD, et al.,

Plaintiff-Appellants,

-against-

ERNST & ERNST, et al.,

Defendants-Appellees.
----- X

SUPPLEMENTAL BRIEF OF APPELLEES

ANDERSON RUSSELL KILL &
OLICK, P.C.
Attorneys for Defendant-
Appellee Peter R. Shaddick
630 Fifth Avenue
New York, New York 10017
(212) 397-9700

DEWEY, BALLANTINE, BUSHBY,
PALMER & WOOD
Attorneys for Defendant-
Appellee Harold V. Gleason
140 Broadway
New York, New York 10005
(212) 344-8000

PIRROTTI & IMPERATO
Attorney for Defendant-
Appellee Robert Panepinto
1501 Avenue U
Brooklyn, New York 11229
(212) 645-3100

BATTLE, FOWLER, LIDSTONE,
JAFFIN, PIERCE & KHEEL
Attorneys for Defendant-
Appellee Paul Luftig
280 Park Avenue
New York, New York 10017
(212) 949-8334

DIFALCO FIELD & LOMENZO
Attorneys for Defendant-
Appellee Carlo Bordoni
605 Third Avenue
New York, New York 10016
(212) 986-2434

POLETTI FREIDIN PRASHKER
FELDMAN & GARTNER
Attorneys for Defendant-
Appellee Howard Crosse
1185 Avenue of the Americas
New York, New York 10036
(212) 730-7373

DAVIS POLK & WARDWELL
Attorneys for Defendant-
Appellee Ernst & Ernst
One Chase Manhattan Plaza
New York, New York 10005
(212) HA 2-3400

MUDGE ROSE GUTHRIE &
ALEXANDER
Attorneys for Defendant-
Appellee Michele Sindona
20 Broad Street
New York, New York 10005
(212) 422-6767

STROOCK & STROOCK & LAVAN
Attorneys for Securities
Industry Association and
Twenty-Five Broker-Dealers,
as Amici Curiae
61 Broadway
New York, New York 10006
(212) 425-5200

TABLE OF CONTENTS

	<u>Page</u>
PRELIMINARY STATEMENT	1
ARGUMENT	2
APPLYING THE TEACHING OF <u>SANDERS v. LEVY</u> TO THE RECORD BEFORE THIS COURT, JUDGE PLATT'S DECISION IMPOSING THE COSTS OF IDENTIFICATION ON THE CLASS REPRESENTATIVES IN THE FIRST IN- STANCE SHOULD BE AFFIRMED AS A PROPER EXERCISE OF THE DISTRICT COURT'S BROAD DISCRETION UNDER RULE 34, FED. R. CIV. P.	
1. Discovery from Non-Parties	6
2. Nature of the "Documents to Be Produced in Order to Identify "Street Name" Purchasers	8
3. Adequacy of Notice	9
4. Other Dispositive Factors in <u>Sanders v. Levy</u> Which are Not Present Here.	10
CONCLUSION	11

TABLE OF AUTHORITIES

Cases:

<u>Eisen v. Carlisle & Jacquelin,</u> 417 U.S. 156 (1974)	4
<u>Sanders v. Levy, No. 75-7608</u> (2d Cir., June 22, 1977), (<u>en banc</u>)	<u>passim</u>
<u>Sanders v. Levy, No. 75-7608,</u> 21 F.R. Serv.2d 1213 (2d Cir., June 30, 1976)	5
<u>Sanders v. Levy, 20 F. R. Serv.2d</u> 1218 (S.D.N.Y. May 15, 1975)	1, 3, 4, 10
<u>Ulrich v. Ethyl Gasoline Corp.,</u> 2 F.R.D. 357 (W.D. Ky. 1942)	6

Page

Statutes and Rules:

Federal Rules of Civil Procedure
Rule 23(c)(2)
Rule 34(a)

3,4,9
3,5,7,8,
9

Miscellaneous:

Advisory Committee Note to
Rule 34(a), 48 F.R.D. 459
(1970)

5

5A Moore, Federal Practice
¶45.05 [1] (1975 ed.)

6

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

- - - - - x

IN RE :
FRANKLIN NATIONAL BANK SECURITIES :
LITIGATION :

No. 76-7616

- - - - - x

ROBERT GOLD, et al., :

Plaintiffs-Appellants, :

-against- :

ERNST & ERNST, et al., :

Defendants-Appellees. :

- - - - - x

SUPPLEMENTAL
BRIEF
OF
APPELLEES

PRELIMINARY STATEMENT

Appellees, joined by the amici curiae, have requested leave to file this Supplemental Brief to discuss the relevance of this Court's recent en banc decision in Sanders v. Levy, No. 75-7608 (2d Cir. June 22, 1977), aff'g 20 F. R. Serv.2d 1218 (S.D.N.Y. May 15, 1975) (Griesa, J.), to this appeal. Our position, as hereinafter more fully set forth, is that, on the very different facts of this case, the principles of law enunciated in Sanders v. Levy support affirmance of the order here appealed from.

ARGUMENT

APPLYING THE TEACHING OF SANDERS v. LEVY TO THE RECORD BEFORE THIS COURT, JUDGE PLATT'S DECISION IMPOSING THE COSTS OF IDENTIFICATION ON THE CLASS REPRESENTATIVES IN THE FIRST INSTANCE SHOULD BE AFFIRMED AS A PROPER EXERCISE OF THE DISTRICT COURT'S BROAD DISCRETION UNDER RULE 34, FED. R. CIV. P.

The question presented to this Court sitting en banc in Sanders v. Levy was

"whether, under the Federal Rules of Civil Procedure, the district court was empowered to order a defendant at its own expense to cull from its computerized records the names and addresses of the members of the class represented by plaintiff."

Slip. Op. at 2-3.^{1/} The Court answered that question in the affirmative and held that, on the particular facts before it, the District Court did not abuse its discretion in requiring the defendant mutual fund to bear that expense, id. at 3, 7, 9. Specifically, Sanders v. Levy held that (1) the names and addresses of members of a class are "discoverable information" which may be obtained by the class representatives from a party defendant pursuant to Rule 34(a); (2) allocation of the cost of such production, specifically the creation of a new computer program to produce the desired information, rests in the sound discretion of the District

^{1/} References are to the typewritten opinion filed June 22, 1977.

Court; and (3) where the particular costs involved were necessitated by the defendants' proposed definition of the class, it was not an abuse of discretion to impose the cost on the party seeking the more inclusive definition.

The question on this appeal is whether the District Court abused its discretion in refusing to require non-party brokers and other nominees to bear the costs of identifying class members whose securities were held in "street" name for the purpose of the individual notice required by Rule 23(c)(2). We respectfully submit that, on the basis of Fed. R. Civ. P. 34(a) as interpreted in Sanders v. Levy, the District Court did not abuse its discretion in ordering the class representatives to advance the costs of identification in the first instance and that, on the facts of this case, nothing in Sanders v. Levy requires a different result.

The facts of Sanders v. Levy, as stated in the District Court opinion, 20 F.R. Serv.2d 1218 at 1220-21, were as follows: plaintiffs, who were shareholders of defendant Oppenheimer Fund, sued its management, investment adviser and others, alleging violations of the federal securities laws by overvaluation of portfolio securities, resulting in inflated prices paid by the class and excessive fees to the investment adviser. Plaintiffs originally sought to represent all persons who purchased shares of the Fund

during a 25-month period, including those who had subsequently sold. Identification of members of the class as so defined required creation of a special computer program, at a cost of approximately \$16,000. In order to avoid this expense, plaintiffs sought to redefine the class to exclude purchasers who had subsequently sold their shares, and proposed to include the Rule 23(c)(2) class action notice in a regular mailing to current shareholders of the Fund. Defendants opposed the proposed redefinition of the class, both because it would limit the res judicata effect of the eventual judgment and because they wished to avoid the adverse effect of mailing the class action notice to current Fund shareholders who were not members of the class. Adopting the broader class definition advocated by defendants, Judge Griesa ruled that the Fund must consequently bear the expense of identification necessary to permit individual notice to the members of the class as so defined, on the ground that "here the expense is relatively modest and it is defendants who are seeking to have the class defined in a manner which appears to require the additional expense." 20 F. R. Serv.2d at 1221.

On appeal, a divided panel of this Court held that the cost of identification was part of the cost of notice which, following Eisen v. Carlisle & Jacquelin,

417 U.S. 156 (1974), could not be imposed upon the defendant Fund, Sanders v. Levy, (2d Cir. June 30, 1976), slip. op. at 4587-88, 21 F. R. Serv.2d 1213, 1218. On reconsideration en banc, a divided Court held that "Federal Rule of Civil Procedure 34 provides the basis for requiring the fund, at its own expense, to provide plaintiffs with discoverable information contained in its computerized records," Sanders v. Levy, (2d Cir. June 22, 1977) (en banc), slip. op. at 6. Because only computer-stored information was at issue in that case, the majority opinion placed particular reliance on the specific language of Rule 34(a) which provides that "documents" required to be produced thereunder must be "translated, if necessary, by the respondent through detection devices into reasonably useable form" and the comment of the Advisory Committee that "in many instances, this means that respondent will have to supply a print-out of computer data," slip. op. at 7, quoting 48 F.R.D. 459, 527 (1970). While specifically acknowledging that Rule 34 permits the expense of special computer programming to be shifted to the discovering party in certain circumstances (ibid.), and eschewing any "inflexible rule" as to who should bear the expense (id. at 8), the Court held that, on the record before it, Judge Griesa did not abuse his discretion in declining to impose the costs of identifying the class members upon the plaintiffs, id. at

7, 9, specifically because the cost of identification there at issue "was occasioned by the court's agreement with defendant that the fund would have been harmed by the proposed class redefinition," id. at 11.

Applying the principles on which Sanders v. Levy was decided to the facts of this case, it is abundantly clear that Judge Platt did not abuse his discretion in holding that the cost of identifying the beneficial owners of securities held in "street" name must be advanced in the first instance by the class representatives, rather than shifted to the non-party brokers and other nominees. The record on which Judge Platt exercised his discretion here differed from the situation before Judge Griesa in several important respects.

1. Discovery from Non-Parties. The Court in Sanders acknowledged that even as to discovery from parties, the District Courts have power in appropriate circumstances to require the costs of special computer programming to be borne by the party seeking the information, slip. op. at 7. That same power exists, a fortiori, to protect a non-party witness from whom voluminous discovery is sought, see 5A Moore, Federal Practice ¶45.05[1] (1975 ed.), quoted in the brief of the amici curiae herein, p. 24; Ulrich v. Ethyl Gasoline Corp., 2 F.R.D. 357 (W.D. Ky. 1942), discussed in the amicus

brief, p. 25. The question of who must bear the expense of discovery from non-parties was not before the Court in Sanders v. Levy, where the mutual fund from whom discovery was sought, although not sued on the class claims, was a defendant as to the companion derivative claims and therefore clearly a "party" within the meaning of Rule 34(a). Here, the information necessary to identify the class members is in the hands of strangers to this litigation. Not only are the brokers not parties to this litigation; they have no relationship to either the definition of the class which creates the need to identify the class members, or to the underlying claims sought to be asserted on behalf of the class. To the extent that they have a relationship with individual members of the class, long-standing public policy expressed in the SEC's proxy rules and the rules of the various securities exchanges requires persons seeking to communicate with beneficial owners to compensate the brokers, see appellee's brief, pp. 21-22; amicus brief, pp. 34-36. The fact that these non-party brokers and other nominees "are not as involved as the mutual fund might be said to have been in the Sanders case" was one of the principal bases of Judge Platt's decision that the costs of identification should not

be shifted to the brokers here (A226), and, we submit, was correct.

2. Nature of the "Documents" to Be Produced in Order to Identify "Street Name" Purchasers. In Sanders v. Levy, the names and addresses of all the members of the class were retrievable from a single computerized source. The Court found that this was precisely the situation to which the language of Rule 34(a) requiring "transla[tion] by the respondent ... into reasonably useable form" was directed. Here, there is no basis for believing that all of the approximately 661 nominees from whom identities of class members must be sought (see A288) maintain computer-stored records of this information. Where brokers' records for the period here in question are not computerized, identification of class members for whom such brokers purchased in "street" name requires a painstaking process of reconstruction from the brokers' stock record books, followed by matching of the account numbers so identified with the actual names and addresses of the brokers' customers (see A208; see also the discussion in the brief of the amici curiae herein, pp. 5-6). This compilation can and arguably should be done by the discovering party from the underlying records (see A208). It is thus doubtful whether the manual

compilation of this information from existing written records may be deemed "transla[tion] ... through detection devices into reasonably useable form" which maybe compelled pursuant to Rule 34(a). Assuming, arguendo, that the information contained in brokers' non-computerized records is discoverable under Rule 34, it is certainly within the discretion of the Court to shift the expense of that task to the party seeking the information. That is precisely what Judge Platt did here.

3. Adequacy of Notice. In Sanders v. Levy, all of the information necessary to identify all of the members of the class was contained in the computerized records maintained by a single party, defendant Oppenheimer Fund. Here, by contrast, the identities of class members must be culled from the records of at least 661 nominees (R 288). If the successful completion of this task must await the disposition of numerous individual proceedings either to compel compliance with subpoenas or determine the allocation of costs in individual instances, the notice to the class required by Rule 23(c)(2) and due process must necessarily be either delayed or inadequate. Judge Platt's order imposing the costs on the class representatives in the first instance avoided all of these complex, time-consuming and expensive problems of judicial administration, and was

designed to help assure the constitutional adequacy of the notice. As such, it was a proper exercise of the Court's discretion, particularly in view of the power of the Court to impose such costs ultimately on the defendants in the event that the plaintiffs should ultimately prevail herein, see Sanders v. Levy, slip. op. at 11-12 and authorities there cited.

4. Other Dispositive Factors in Sanders v. Levy Which Are Not Present Here. Judge Griesa's decision to impose the costs of identification on the mutual fund in Sanders v. Levy was based primarily on the ground that those costs were necessitated by the broader definition of the class which defendants had urged, over plaintiffs' objection, 20 F. R. Serv.2d at 1221. This Court's holding that that decision was not an abuse of discretion was squarely based on the same grounds, slip. op. at 10-11. No such special facts are present here. The non-party nominees, to whom plaintiffs propose to shift the cost of identification of class members, have no interest in this litigation and no connection with the definition of the class. There is no basis whatsoever for holding that Judge Platt abused his discretion in imposing such costs on plaintiffs in the very different circumstances of this case.

CONCLUSION

In reviewing Judge Griesa's exercise of his discretion in allocating the costs of discovering the identity of class members in Sanders v. Levy, the Court sitting en banc emphasized that "there is no warrant for applying an inflexible rule that the discovering party bear the expense," slip. op. at 8. There is similarly no warrant for applying an inflexible rule that the discovering party be relieved of the expense. Judge Platt's order requiring the class representatives to advance such expenses in the first instance, on the facts of this case, was well within that discretion. The order appealed from should be affirmed.

Dated: New York, New York
July 1, 1977

Of counsel:

Barbara A. Lee

ANDERSON RUSSEL KILL &
OLICK, P.C.
Attorneys for Defendant-
Appellee Peter R. Shaddick
630 Fifth Avenue
New York, New York 10020
(212) 397-9700

Respectfully submitted,

POLETTI FREIDIN PRASHKER
FELDMAN & GARTNER
Attorneys for Defendant-
Appellee Howard D. Crosse
1185 Avenue of the Americas
New York, New York 10036
(212) 730-7373

BATTLE FOWLER LIDSTONE
JAFFIN PIERCE & KHEEL
Attorneys for Defendant-
Appellee Paul Luftig
280 Park Avenue
New York, New York 10017
(212) 949-8334

(continued)

DAVIS POLK & WARDWELL
Attorneys for Defendant-
Appellee Ernst & Ernst
One Chase Manhattan Plaza
New York, New York 10005
(212) HA 2-3400

DiFALCO FIELD & LOMENZO
Attorneys for Defendant-
Appellee Carlo Bordoni
605 Third Avenue
New York, New York 10016
(212) 986-2434

PIRROTTI & IMPERATO
Attorneys for Defendant-
Appellee Robert Panepinto
1501 Avenue U
Brooklyn, New York 11229
(212) 645-3100

DEWEY, BALLANTINE, BUSHBY,
PALMER & WOOD
Attorneys for Defendant-
Appellee Harold V. Gleason
140 Broadway
New York, New York 10005
(212) 344-8000

MUDGE ROSE GUTHRIE & ALEXANDER
Attorneys for Defendant-
Appellee Michele Sindona
20 Broad Street
New York, New York 10005
(212) 422-6767

STROOCK & STROOCK & LAVAN
Attorneys for Securities Industry
Association and Twenty-Five
Broker-Dealers, as Amici Curaie
61 Broadway
New York, New York 10006
(212) 425-5200